# United States
# Circuit Court of Appeals
## For the Ninth Circuit.

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| THOMAS W. NEALON, Trustee, and J. J. MACKAY, Creditor, *Appellants,* *vs.* GEORGE W. SHUTE, Bankrupt, *Appellee.* | No. 5949. |

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**Appeal from the United States District Court for the District of Arizona.**

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## REPLY BRIEF OF APPELLANTS.

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WILLIS N. BIRDSALL,
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on the Brief.

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THOMAS W. NEALON, Trustee, and J. J. MACKAY, Creditor,

Appellants,

vs.

GEORGE W. SHUTE, Bankrupt,

Appellee.

Appeal from the United States District Court for the District of Arizona.

### REPLY BRIEF OF APPELLANTS.

Counsel for appellee in stating the nature of the case, pages 2, 3 and 4 of their brief, have cited part of the record without including other parts needed to convey accurate information on the points covered, and while it is perhaps immaterial in any event, counsel for appellants deem it wise to present to the court such further citations as will make the matters referred to clear and thus avoid misapprehension as to the true facts.

On page 2 of appellee's brief appears what purports to be a stipulation entered into on January 3d appearing in Volume 1, page 109, of the transcript as follows:

> "That the court may have the transcript of testimony taken before the referee for review before hearing."

Counsel for appellee, however, omit to cite several other stipulations preceding the one cited and entered into at the same time, the first of which reads as follows:

> "That all depositions and testimony heretofore introduced in evidence before the referee may be admitted *in so far as pertinent.*" (Italics ours.)
>
> (Trans., Vol. 1, p. 109.)

It might appear from the statement of appellee that a stipulation had been entered into by counsel by which it was agreed that Judge Sawtelle should read and consider all testimony taken before the referee whether or not pertinent to the issues involved on the hearing on discharge. As will be seen by the record this is not a fact. A stipulation was merely made permitting Judge Sawtelle to take the referee's files in the case to Tucson for examination before the trial, such stipulation following the one made that on the hearing depositions and testimony before the referee, "so far as pertinent," might be admitted. We are unable to determine from the language of appellee whether it was intended to create the impression that the trial court reviewed and considered in reaching his conclusions matters appearing in the referee's files "not pertinent" to the issues on discharge, and not introduced in evidence, and that the entire record

considered by the trial court is not here, but clearly such inference is deducible from the language used by appellee, and is not in accord with the facts, which we deem should be made clear. Reference is made to the order approving the statement of evidence appearing in Volume 2, page 842, of the Transcript, wherein Judge Sawtelle certified that the statement of evidence with amendment attached contains "all of the testimony in the case." Certainly this court and all parties are bound by this certification by the trial judge, and the impression seemingly intended to be created by the language of the appellee that the entire record considered by the trial court is not before this court is dissipated. In view of this certification of Judge Sawtelle we are unable to determine why appellee inserted on page 3 of its brief,

> "The record does not show the names of the witnesses whose testimony was taken before the referee nor the nature of the exhibits attached to the transcript of their testimony; neither does the transcript show that it contains all of the testimony so reviewed by the judge before hearing."

Obviously, the record here would contain neither a list of witnesses whose testimony had been taken before the referee on other matters, nor a description of the exhibits which might be attached to evidence taken before the referee. This proceeding was an original hearing before the court on the matter of the discharge of the bankrupt and had

neither been referred nor had any evidence been taken in same prior to the ninth day of January, 1929, and no evidence was introduced except as it appears in this record. On the trial appellants produced certain witnesses who had testified before the referee, and in order to save the time of the court it was stipulated that their evidence before the referee should be admitted in this proceeding, and that they would be examined before the court only as to any new matters concerning which appellants desired testimony. This was true of the witnesses George F. Wilson, E. A. Wedepohl and Sylvan Ganz, all of whom were in court. (Trans., Vol. 1, pp. 111, 263, 233 and 243.) The same stipulation was made with respect to the testimony of Jessie M. Shute, wife of the bankrupt (Trans., Vol. 1, p. 132), and the testimony of A. E. England, who was under subpoena, but was unable to appear by reason of illness. (Trans., Vol. 1, p. 361.) Appellants on the trial attempted to offer in evidence certain testimony of the bankrupt given before the referee during various examinations as admissions against interest. The trial judge as shown by transcript, Volume 1, page 301, directed appellants to offer the document as a whole, stating that he would read it and pick out the admissions against interest and later, and at the conclusion of the cross-examination of the bankrupt, appellants offered *all* the testimony of the bankrupt given before the referee as a part of their case and the same was admitted. (Trans., Vol. 2, p. 676.) If any testimony of any witness taken before the referee

was "pertinent," counsel for appellee had the same opportunity to offer it in evidence as had the appellants to offer the parts they desired.

We are, therefore, at a loss to understand the following language on page 4 of appellee's brief:

> "In addition to original testimony taken before the court there were also introduced in evidence transcripts of all the testimony of Judge Shute and that of *some* of the other witnesses taken before the referee."

We sincerely trust it was not the intention of counsel for appellee to insinuate that the trial judge based his conclusions on matters outside the record after having certified that the record contained all the testimony considered by him.

Appellee, on page 10 of his brief, seeks to distinguish the case of Milkman vs. Arthe, 221 Fed. 134, on the ground that the question raised was not false swearing or opposition to discharge. The case, however, directly holds that the fact that a wife saved money from her household allowance or money handed to her by her husband did not make it her separate property. The case at bar is even stronger than the Milkman vs. Arthe case, *supra,* for in the case at bar the bankrupt testified that money from his earnings was placed in a joint account so either could check against it. Also see income tax return for 1927, in which a $1200 loss paid out of this savings account in February, 1928, is deducted as a separate loss of the bankrupt, thirty-two days before adjudication of bankruptcy. (Trans., Vol. 2, p. 804.)

The two Arizona cases on page 15 of appellee's brief holding that a conveyance of community property from one spouse to the other changes its character from community to separate property correctly state the law. In neither case, however, was the grantor insolvent.

The case of In re Crenshaw, 95 Fed. 632, quoted on page 15 of appellee's brief, merely holds that the transfer in that case having been made more than four months before the petition in bankruptcy is not declared null and void by the Bankruptcy Act.

In the case of In re Howell, 105 Fed. 504, cited by appellee on page 16 of his brief, the fact showed that the property involved (being $20,000 in cash) had been conveyed to the wife *nine years* before the bankruptcy, and that a creditor's bill had been filed several years before, which was still pending, for the recovery of this property. The Court held that under the facts, the property need not be scheduled. The community property law was not involved.

In the Morrow case, 97 Fed. 574, cited by appellee (page 17 of brief) on the question of fraudulent intent, the facts were stipulated that Nancy Morrow (the bankrupt) had never claimed nor *believed she had the right to claim* the property omitted from her schedules, since the partition of her father's estate, and on such stipulation as to her *belief,* the Court held there was no fraudulent intent on her part, even though she in fact had an interest in the property.

While it is true that in the Spiroplos case, cited by appellee on page 18 of his brief, this Court held that the trustee had not sustained the burden of establishing that the bankrupts had concealed property with fraudulent purpose, a perusal of that case shows no similarity between the actions of the bankrupts there and those of the bankrupt in the instant case. In fact the very language used there, namely, "Omissions to set forth the transactions complained of are more easily attributed to honest than dishonest purposes," distinguishes the whole matter from the issues here. If there is a single omission in the case at bar which points to an honest rather than a dishonest purpose, we have failed to perceive it. Every omission and concealment charged was in the interest of the bankrupt, and the sum of over $2,000 had already been brought into the estate which would have been lost had no investigation been made. It is noticeable that the bankrupt never "omitted" to claim an exception or a privilege in his own interests.

Appellee next cites the Carlson case, 18 Fed. 103, and quotes at length therefrom on pages 21 and 22 of his brief on the character of evidence necessary to sustain a finding of making a false oath. It will be recalled that in that case the Court stated that while not satisfied with the evidence, he could not find that the bankrupt had wilfully made a false oath or concealed property, citing the fact that the bankrupt was an ignorant person, who imperfectly understood English, and that it was extremely diffi-

cult in such circumstances for correct schedules to be made.

The case of Humphries vs. Nalley, 269 Fed. 607, is cited by appellee on page 22 of brief on the same matter of false oath. A reading of the case shows no slightest resemblance to the facts here. In that case the bankrupt was a laborer who omitted from his schedules $30 in money (which he used for his filing fees), a watch and household furniture valued at from $100 to $125, all of which were exempt. The Court held the omission not intentional, as he had signed the schedules prepared for him and testified fully and freely at the first meeting. Had the bankrupt in the instant case omitted to schedule only exempt property, this matter would undoubtedly not be pending here. That was property he remembered perfectly and he had no hesitation in scheduling it and claiming the exemption therefor.

Referring to the Weiner case, cited by appellee on page 24 of brief, on the matter of keeping books, the citation therefrom is correct so far as it goes. If intended to leave the impression, however, that a discharge was granted in that case, *that* is erroneous, for a discharge was there denied. We therefore supplement the quotation of appellee with this language, immediately following that quoted:

> "On the other hand, the election to keep them implies that they, if not by themselves, then in conjunction with other less formal records shall *prima facie* give every evidence of an hon-

> est effort to reflect the *entire business* of the bankrupt. As long as there is any doubt on this point, *a court of bankruptcy should resolve that doubt for the benefit of creditors.* A discharge is a privilege granted by the Act. One who seeks thereby to avoid his debts, *must comply strictly with its provisions.*" (Italics ours.")

The Merritt case, decided by this court, upheld the discretion of the trial court in refusing a discharge to a bankrupt whose fraud it seems to us was not nearly as flagrant as that of the bankrupt in the case at bar, and the case from the Eighth Circuit, Barton Bros. vs. Texas Produce Co., 136 Fed. 355, was in the same category. In both of those cases was stressed the absolute necessity of a full surrender of property and a frank disclosure of his affairs by the bankrupt before a discharge would be granted.

The statement of counsel for appellee on page 27 of appellee's brief that the Transcript does not contain all of the testimony read and considered by the trial court, as heretofore pointed out herein, is contrary to the facts and obviously misleading. We refer again to the certification of Judge Sawtelle appearing on page 842, Volume 2 of Transcript that the statement of evidence contains *all of the testimony in the case.* No stipulation was made or *intended* that Judge Sawtelle was to take the record of the referee to Tucson for any other purpose than to "review" same to familiarize himself with the proceedings had before the referee, and

it was clearly understood by the Court and *all parties* that all evidence considered on the hearing was introduced on the hearing. Judge Sawtelle's understanding is clearly indicated by his language on page 301, Volume 1 of the Transcript.

Referring to appellee's statements on page 18 of his brief, that the trustee testified (Vol. 2, p. 439 et seq., Trans.) that "notwithstanding he had been trustee for approximately a year and eight months he had never instituted any suits or taken any action in a court of competent jurisdiction to recover the numerous items of property which he claimed had been fraudulently conveyed, given away and knowingly and fraudulently concealed," we respectfully submit that an examination of the record will show that this statement of appellee is not in accordance with the facts and that the trustee did *not* so testify.

In the first place, the record shows that the trustee was elected at the first meeting of creditors on May 1, 1928 (Trans., Vol. 2, p. 698), and that therefore at the time of this hearing on January 9, 1929, only *eight* months had elapsed since his election instead of *a year and eight months,* as asserted by appellee. Furthermore it appears from the record that as to four items of property (the savings account and the Essex car being two, and the trustee not being permitted by Mr. Moore, counsel for appellee to finish his sentence and tell what the other two were (Trans., Vol. 2, p. 439), orders to show cause why turnover orders should not be made were then pending before the referee. It further ap-

pears (Trans., Vol. 2, pp. 441 and 262), that both the Creed and Noble notes were for the first time even seen by the trustee in court at this hearing, their production having theretofore been refused. The trustee further testified that he contemplated proceedings on both the Goswick and the Globe property the nature of which he refused to disclose (Trans., Vol. 2, pp. 457, 458), and it must be kept in mind that knowledge of the Goswick transaction first came to the trustee Thanksgiving week, only two or three weeks before the specifications of objection to discharge were filed; that it had been necessary to take the deposition of Mary E. Holmes in Boston in September, 1928, to obtain information regarding the mortgage on the Globe property *not* furnished by the bankrupt after request for it (Trans., Vol. 2, p. 798), and that bankrupt's wife had been examined regarding the Globe property and other property in order to obtain further necessary information late in November, 1928. (Trans., Vol. 1, p. 167.) It is also shown by the record that each and all of these examinations disclosed wide discrepancies in matters formerly testified to by the bankrupt and that the trustee was still conducting examinations at the time the specifications of objection to discharge were filed on December 19, 1928. It should be further borne in mind that the bankrupt had filed his petition for discharge on May 29, 1928, on the day when he first produced for the trustee *any* records, save a few checks, and those few and incomplete, and before the trustee had had opportunity to examine those records and question the

bankrupt concerning same, and before the examinations had been completed which resulted in the ascertainment of the true facts regarding the status of the Hudson car and the life insurance policy, and the recovery of those items for the bankrupt's estate.

The examination of the bankrupt was not concluded at the time the specifications of objection to discharge were filed on December 19th, but on December 27th, *eight days after* the filing of the specifications of objection to discharge, he for the first time gave testimony concerning certain transactions and produced an incomplete statement of his alleged financial transactions. (Trans., Vol. 2, p. 810 et seq.)

To hold that the fraudulent concealment of property could not be urged as a bar to a discharge unless and until suits to recover the property concealed or fraudulently transferred had been instituted would certainly be nullifying the provisions of the act, and such is not the holding of the courts. Obviously where, as is often the case, there are few if any assets in the bankrupt's estate, creditors need not advance money for costly litigation in order to place themselves in a position to assert the rights given them under the act itself of objecting to a discharge on the ground that property has been concealed from the estate. As was said by the Court of Appeals for the Sixth Circuit in Devorkin vs. Security Bank, etc., 243 Fed. 171:

> "In deciding whether the conveyance had the effect to hinder, delay and defraud creditors, it

is of no controlling importance that the trustee had not been able to avoid it, or even that he had not tried to avoid it."

But apart from the misstatement of the facts and of the testimony of the trustee in the language quoted above from appellee's brief, and notwithstanding that the right to oppose discharge on the ground of fraudulent concealment in nowise depends upon the institution of actions to recover the property, the fact remains that the situation respecting the nine items on which appellee claims no actions for recovery had been instituted in "competent courts" at the time of this hearing was as follows: As to three of these items, namely, the Hudson car, the life insurance policy and the $250 La Prade deposit, they had all been recovered for the estate *without* litigation. As to two other items, the savings account and the Essex car, orders to show cause why turnover orders should not be made were then pending before the referee. As to the phonograph, the bankrupt had at one time promised to surrender that, without action being taken (Trans., Vol. 2, p. 788). And as to the other three items, the Globe property, the Goswick matter, and the $995 Wentworth payment, the trustee testified he had in mind the procedure he intended to follow. (Trans., Vol. 2, pp. 457, 458.) In addition to this two other orders to show cause why turnover orders should not be made were pending before the referee.

Just what the bankrupt considers a "court of competent jurisdiction" we are unable to determine. While *he* was the one who voluntarily in-

voked the jurisdiction of the Bankruptcy Court, to secure for himself release from his indebtedness, he seemingly resents the application of the provisions of the act requiring the surrender of his property and assets and a full and frank disclosure of his affairs as a condition precedent to discharge from his debts. His attitude from the time he adopted bankruptcy as, to use his own language, "the easiest way," has been not only indifferent, but scornful in meeting the obligations placed upon him by the provisions of the act. Since the magnificent gesture with which he filed his voluntary petition in bankruptcy, accompanied by schedules listing only one creditor with an indebtedness of over $31,000, and total nonexempt assets (not even listing his 25 per cent interest in the firm of which he was a member) of $15.67 cash and a lot at Globe valued by him at $250, against which were unpaid taxes of $45), (Trans., Vol. 1, pp. 199–202), he has cheerfully and voluntarily done only one thing in accordance with the provisions of the act—viz., to file his petition for discharge less than six weeks after his adjudication. Every other action taken and every disclosure made, resulting in the recovery for the estate at the time of this hearing of over $2,000, besides the 25 per cent interest in his law firm, were the result of orders of the Court or the persistent and painstaking efforts of the trustee, or both. He forced the trustee to consume months of time and conduct expensive examinations of many witnesses and records in order to obtain information as to property concerning which frank

disclosure should have been made by him in the first instance, and he now even assumes to dictate the manner in which the trustee shall proceed in recovering assets of the estate and to object because the latter has not commenced litigation in other courts to recover property, the very existence of some of which was unknown to the trustee until a short time before this hearing. Is it not a fair inference that this bankrupt all the way through was determined to make the recovery of any property so costly (with at the start only $15.67 available in the estate) that the creditor would be discouraged at the outset and no investigation would be made?

We know of neither rule of law nor dictate of equity which requires a trustee in bankruptcy, whose duties are plain and fixed by the act, and who is under the direct supervision of the referee, to consult the pleasure or wishes of the bankrupt as to the time, place or method of his procedure to recover concealed assets, and certainly ordinary prudence would suggest to a trustee the inadvisability of taking the bankrupt into his close confidence on matters pertaining to the recovery of such assets, where the concealment has been conceived and carried out by the bankrupt himself.

In the closing peroration in their brief, counsel for appellee seemingly advance the, to appellants, most remarkable inference that the trial judge had personal knowledge of the parties here (assuming that by the word "actors" was meant the parties and their counsel), which he considered in reaching his conclusions, rather than, or in addition to, the

record before him. Possibly we mistake the intentions of counsel for appellee, but we can gather no other meaning and we refer to it only to say that if such *was* their belief and their intention was to convey that belief, it should be urged rather as a reason for reversal of the trial court's decision than for sustaining it.

Appellants cannot see that knowledge—or belief of knowledge—since it is given to none to read the hearts and motives of others except as they are revealed by actions and deeds—of any or all of the parties concerned in litigation could ever be considered a safe criterion in guiding a trial court in reaching a decision, and we can hardly believe that counsel for appellee so meant to contend.

Appellants are willing that this court shall determine the "manner of men" (and women), who are what appellee terms "actors" in this proceeding from the cold facts shown by this record.

That record will disclose the objecting creditor as the man who in 1918 signed as surety the note of his then friend for $20,000, and as a result thereof suffered a financial loss in payment of the note and interest (no part ever being paid by the bankrupt) of over $31,000.00 (Trans., Vol. 1, pp. 179–190) and who finally and in 1927, unable to obtain any satisfaction, placed the matter in the hands of an attorney for collection. It discloses the attorney for that creditor in June, 1927, agreeing with the bankrupt to withhold suit until after October 1st, 1927, in consideration of a waiver of the statute of limitations which was running against the debt (Trans., Vol. 1,

p. 189), and who negotiated with the bankrupt over a period of several months in an endeavor to reach an amicable settlement of the indebtedness; who, in fact did not bring suit for the recovery of the amount due this creditor until April, 1928, and after the bankrupt had refused to make settlement of the entire indebtedness on a basis of payment of $6,000. (Trans., Vol. 2, p. 792.) It discloses the bankrupt as a man who, with a net income in excess of $18,000 for the year 1927, not only refused to settle this claim for $6,000 but refused to pay as much as $100 a month on same (Trans., Vol. 2, p. 746), who after securing the extension of time before suit would be filed in June, 1927, proceeded during the months intervening before bankruptcy to place earnings and property, as he believed, outside of the reach of this creditor; who put a conditional sales contract in November, 1927, on a car which was then completely paid for, because, as he says on his examination, he expected he would have trouble with this creditor (Trans., Vol. 2, p. 539), who testified at the examination before the referee he "had made up his mind he (Mackay), would never get a look-in" (Trans., Vol. 2, p. 791); who admitted on examination that he held a $6,000 dividend paid by his firm in June, 1927, out of his bank account and purchased cashier's checks to cover the amount because he was negotiating a settlement of an indebtedness in excess of $7,000 with the Old Dominion Bank of Globe for $2,200, and he feared he would lose his settlement if the bank knew of this payment (Trans., Vol. 2, p. 829); who under oath

on May 1st testified he owed about $1,000 on his Hudson car and that he had turned it back to England, the dealer (Trans., Vol. 2, pp. 710, 711), when in fact the car was entirely paid for, and who subsequently testified that he expected to get the car back and pay it out, "but not for someone else's benefit" (Trans., Vol. 2, p. 737); who admits making oath to income tax returns, schedules and an answer in a suit in which he was defendant involving real estate in Yavapai County, in all of which were statements he now says are untrue; who swore under examination in the referee's court that he had not received any amount but $500 from Goswick, when in fact he had received in the preceding eighteen months the sum of $3,500 from Goswick. This and numerous other statements in the record reveal the manner of man the bankrupt was and is. The record discloses the trustee as a man who by persistent effort at the time of this hearing had succeeded in already bringing into the estate over $2,000 and a 25 per cent interest in the law firm, none of which had been scheduled and which would have been lost save for his efforts; who because he remained true to his oath and had the temerity to insist that this bankrupt, like *any other person* who invokes this act, must surrender *all* his property and make full and frank disclosure of his affairs, became the object of an attack by bankrupt and his counsel in an endeavor to camouflage the issues and divert attention from the conduct of the bankrupt.

The bankrupt admits the weakness of his own position when instead of pointing out anything in

the record to sustain that position, he attempts by innuendo to attack the good faith of the trustee.

We can readily understand why the activities of the trustee which had forced him to disgorge more than $2,000 at the time of this hearing are particularly obnoxious to the bankrupt, but we submit that all the camouflage in the world cannot obliterate the fraudulent record of the bankrupt himself nor can baseless accusations of others relieve the solemn obligation laid upon him by the Bankruptcy Act.

We believe that the uncontradicted testimony in the record, and the admissions of the bankrupt on his various examinations, leave but one inference to be drawn from the facts thereby established, and that is that the bankrupt knowingly and fraudulently concealed from the Court, the creditor and the trustee, assets belonging to his estate and in pursuance of his scheme to defraud this creditor, he knowingly and fraudulently made false oaths to his schedules and gave false testimony on his examination.

Respectfully submitted;

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